PUBLIC RETIREMENT SYSTEMS OF MONTANA

Four Ways to Modernize Montana's Public Pension Systems

As lawmakers continue to review Montana's largest public pensions and refine recommendations for the 2023 legislative session, some issues stand out as critical items needed to bring multi-generational systems like the Public Employee Retirement System (PERS) and Teachers' Retirement System (TRS) into the 21st Century regarding funding policy and risk management. Using the pension reform objectives listed below, the Pension Integrity Project at Reason Foundation recommends lawmakers review four critical areas to ensure long-term solvency and protect members' retirement benefits.

Objectives

Keeping Promises	Retirement Security	Predictability	Risk Reduction	Affordability	Attractive Benefits	Good Governance
Ensure the ability to pay 100% of the benefits earned and accrued by active workers and retirees.	*Provide retirement security for all current and future employees.*	*Stabilize contribution rates for the long-term.*	*Reduce pension system exposure to financial risk and market volatility.*	*Lower long-term costs for employers, taxpayers, and employees.*	*Ensure the ability to recruit 21st Century employees.*	*Adopt best practices for board organization, investment management, and financial reporting.*

#1 - ADOPT PROPER ACTUARIAL FUNDING

- ✓ The Montana legislature funds the state's public pension systems based on a fixed rate set in statute instead of paying the annual amounts actuaries calculate is necessary to maintain long-term solvency.
- ✓ Despite the legislature having a history of raising contributions in years when requested, those recommendations stem from an "open amortization" policy that resets annually, similar to refinancing a home mortgage every year.
- ✓ 2020 Legislative Fiscal Division: "*...current funding policies leave the systems heavily reliant on investment earnings and* ***unable to adjust contributions to maintain an actuarially sound basis in times of significant financial declines.***"
- ✓ Adopting an actuarially determined funding policy akin to HB323 (2021) would commit the state to fully funding benefits by a set date, allowing the state to systematically pay down its unfunded liability while increasing member confidence in their retirement security.

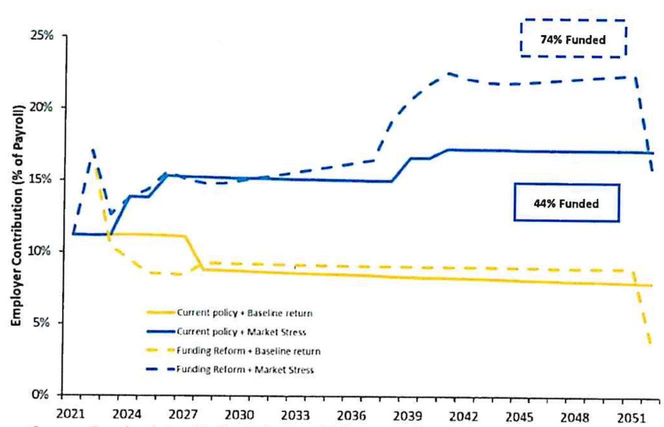
#2 - BUY DOWN RISK

- ✓ Montana's reported $500 million state budget surplus presents lawmakers an opportunity to avoid major interest costs for employers and taxpayers by accelerating the payment of existing unfunded liabilities.
- ✓ Legislators could use one-time surplus funds to buy down the pension systems' investment return assumptions.
- ✓ PERS, for example, could use a $100 million infusion to lower its investment return assumption down ten basis points without increasing the system's reported unfunded liability.

***Did You Know?** While PERS now uses a 7.3% rate, the average US public pension system discount rate has dropped to 7% and continues to fall.*

#3 – STOP PERS DC BENEFIT REDUCTIONS

- ✓ As a result of HB454 (2013), the floating PERS defined benefit (DB) amortization period recently dipping below 25 years threatens to trigger a reduction in the employer contribution rate by 2.27% and 1% from employees, for both the PERS DB and PERS defined contribution (DC) plans.
- ✓ Combining what an employer contributes to a PERS DC member account with the funding status of the DB fund conflates two independent retirement benefits and cuts retirement benefits for over 4,700 PERS DC members.



Source: Pension Integrity Project actuarial forecast of PERS.

#4 – ADD STRESS TESTING TO GREEN SHEETS

- ✓ Instead of only showing a scenario of what the plan's funding would look like if it met its assumed rate of return each year, stress testing explores a range of realistic market scenarios to comprehensively demonstrate what could happen to the pension plan's funding over the next few decades given volatile markets.
- ✓ This testing allows policymakers to see not only where the system's financial health is today, or where it is expected to be in 30 years, but how the system would be impacted in times of unforeseen economic volatility.

PENSION INTEGRITY PROJECT CONTACTS

- Leonard Gilroy, Senior Managing Director (leonard.gilroy@reason.org)
- Steven Gassenberger, Policy Analyst (steven.gassenberger@reason.org)

Reason Foundation is a national 501(c)(3) public policy research and education organization with expertise across a range of policy areas, including public sector pensions, transportation, infrastructure, education, and criminal justice. For more information about the Pension Integrity Project at Reason Foundation, visit reason.org.